Report

of the

Examination of

Church Mutual Insurance Company

Merrill, Wisconsin

As of December 31, 2003

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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October 15, 2004

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Commissioner of Insurance
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Honorable Walter A. Bell
Secretary, Southeastern Zone, NAIC
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State of Alabama
201 Monroe Street, Suite 1700
Montgomery, Alabama 36104

Commissioners:

In accordance with your instructions, a compliance examination has been made of the affairs and financial condition of:

CHURCH MUTUAL INSURANCE COMPANY
Merrill, Wisconsin

and this report is respectfully submitted.

I. INTRODUCTION

The previous examination of Church Mutual Insurance Company (hereinafter CMIC, the company or Church Mutual) was conducted in 1999 as of December 31, 1998. The current examination covered the intervening period ending December 31, 2003, and included a review of such 2004 transactions as deemed necessary to complete the examination.

The examination consisted of a review of all major phases of the company's operations, and included the following areas:

History
Management and Control
Corporate Records
Conflict of Interest
Fidelity Bonds and Other Insurance
Employees' Welfare and Pension Plans
Territory and Plan of Operations
Affiliated Companies
Growth of Company
Reinsurance
Financial Statements
Accounts and Records
Data Processing

Emphasis was placed on the audit of those areas of the company's operations accorded a high priority by the examiner-in-charge when planning the examination. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The section of this report titled "Summary of Examination Results" contains comments and elaboration on those areas where adverse findings were noted or where unusual situations existed. Comment on the remaining areas of the company's operations is contained in the examination work papers.

The company is annually audited by an independent public accounting firm as prescribed by s. Ins 50.05, Wis. Adm. Code. An integral part of this compliance examination was the review of the independent accountant's work papers. Based on the results of the review of these work papers, alternative or additional examination steps deemed necessary for the completion of this examination were performed. The examination work papers contain documentation with respect to the alternative or additional examination steps performed during the course of the examination.

Independent Actuary's Review

An independent actuarial firm was engaged under a contract with the Office of the Commissioner of Insurance. The actuary reviewed the adequacy of the company's loss and loss adjustment expense reserves. The actuary's results were reported to the examiner-in-charge. As deemed appropriate, reference is made in this report to the actuary's conclusion.

II. HISTORY AND PLAN OF OPERATION

The company was organized on March 4, 1897, as the Wisconsin Church Mutual Fire Insurance Association. The company was founded for the purpose of providing insurance under the mutual plan to any church, church society, or pastor of one of the synods constituting the Evangelical Lutheran Synodical Conference, or the Norwegian Evangelical Church of America. It commenced business on June 3, 1897.

A revision of the articles of incorporation adopted at a special meeting of the policyholders held on October 16, 1947, changed the name of the company to the Wisconsin Church Mutual Fire Insurance Company and set forth the following corporate purposes that have continued to the time of this examination:

> "This company is organized for the purpose of insuring upon the mutual plan the members against any of the hazards as may be authorized or permitted for companies of its class under the laws of the state of Wisconsin as they are or may be hereafter amended. This revision in the statement of corporate purpose was made to reflect the diversity of religious denominations the company has begun to serve."

An amendment to the articles of incorporation adopted at the annual policyholders' meeting held March 19, 1952, changed the name to Church Mutual Insurance Company.

The company has been the acquiring party in a succession of mergers during its history. The company absorbed all of the assets and assumed all of the liabilities of the following companies:

- Lutheran Mutual Fire Insurance Company of Burlington, Iowa, on June 11, 1949;
- Mutual Fire Insurance Society of the Michigan Conference of Evangelical united Brethren Church, Ltd., Mount Pleasant, Michigan, on September 1, 1953;
- American Church and Home Mutual Insurance Company of Madison, Wisconsin, on November 30, 1962;
- Cheese Makers Mutual Insurance Company of Madison, Wisconsin, on February 1, 1963; and
- Furniture Mutual Insurance Company of Milwaukee, Wisconsin, on May 31, 1963.

Church Mutual is licensed in all 50 states and the District of Columbia. The company writes significant direct premium in all areas of the country, with the exception of the New England states and Hawaii. The following states accounted for the largest percentage of direct premium written in 2003:

Texas	$ 47,786,741	10.9%
California	38,026,594	8.6
Illinois	22,995,344	5.2
Florida	21,465,121	4.9
North Carolina	20,162,021	4.6
Georgia	17,811,598	4.0
Michigan	17,803,273	4.0
Missouri	16,917,835	3.8
Pennsylvania	16,366,617	3.7
Wisconsin	15,490,560	3.5
All others	205,667130	46.8
Total	$440,492,834	100.0%

The company specializes in providing property and casualty insurance coverages for churches and religious institutions, which also includes clergy dwellings, camp buildings, long-term care facilities, schools, church offices and apartments. Due to the company's local profile in the Wisconsin counties of Lincoln, Marathon, Langlade, Taylor, Vilas, Oneida, and Portage, the company accepts a modest amount of homeowner's risks for residents of those counties. Otherwise, new homeowner's policies are only written for members of the clergy or other employees of religious institutions.

The following table is a summary of the net insurance premiums written by the company in 2003. The growth of the company is discussed in the Financial Data section of this report.

Line of Business	Direct Premium	Reinsurance Assumed	Reinsurance Ceded	Net Premium
Fire	$ 525,549	$ 97,341	$ 129,441	$ 493,449
Allied lines	3,528,024	217,947	2,244,195	1,501,776
Homeowners multiple peril	3,759,270	0	916,076	2,843,194
Commercial multiple peril	307,557,199	0	96,975,169	210,582,030
Inland marine	101,544	0	34,856	66,688
Medical malpractice - Occurrence	2,751,624	0	368,145	2,383,480
Worker's compensation	62,024,979	2,075,000	8,099,119	56,000,860
Other liability – occurrence	18,715,463	0	11,955,527	6,759,936
Other liability - claims made	544,091	0	74,697	469,394
Commercial auto liability	30,020,984	0	4,139,807	25,881,177
Auto physical damage	10,935,600	0	997,048	9,938,552
Fidelity	3,618	0	238	3,380
Burglary and theft	24,889	0	1,274	23,615
Reinsurance - non-proportional assumed liability	0	903,803	64,471	839,332
Total All Lines	$440,492,834	$3,294,092	$126,000,062	$317,786,863

The company's headquarters is located in Merrill, Wisconsin. The major products of the company are marketed through 15 divisional sales offices located in the following cities:

Atlantic Division	Richmond, Virginia
Carolina Division	Greensboro, North Carolina
Central Division	Indianapolis, Indiana
East Central Division	Exton, Pennsylvania
East Texas Division	Plano, Texas
Empire Division	Liverpool, New York
Great Lakes Division	Elgin, Illinois
New England Division	Worcester, Massachusetts
North Central Division	Minneapolis, Minnesota
Ohio Valley Division	Reynoldsburg, Ohio
South Central Division	Kansas City, Missouri
Southeastern Division	Norcross, Georgia
Southern Division	Little Rock, Arkansas
Southwestern Division	Oklahoma City, Oklahoma
West Central Division	Des Moines, Iowa

Each division manager is responsible for a number of states and regional representatives. A total of 44 divisional and satellite offices are under the direction of the division managers. Business is acquired through direct writing regional representatives and through independent agencies.

The company employs approximately 170 regional representatives. Collectively, these employees wrote 80% of the company's premium volume in 2003. In addition to a salary, each regional representative receives a commission of 10% on all new business, increases on renewals, and additions to existing policies as well as a $50.00 bonus for policyholders which renew their business with Church Mutual.

The company has active agreements with 13 agencies, accounting for approximately 20% of the company's premium volume in 2003. Agents receive commissions ranging from 15% to 20% on new and renewal business and commissions ranging from 10% to 23% on worker's compensation business. A contingent commission may also be paid, based on the profitability and volume of the agent's book of business.

Under the Church Mutual Profit-Sharing Plan, all employees with at least one full year of service may receive up to 7% of base salary, depending on the company's level of profitability. Various other incentive programs exist to further reward exceptional performance by the regional representatives, including the Presidential Bonus, the President’s Circle Trip Bonus, the High Career Performance Bonus, and other special bonuses. The Presidential Bonus is paid to regional representatives who exceed a standard of exceptional sales performance set annually by the company's president. The President’s Circle Trip is awarded to regional representatives who meet a minimum premium production goal and meet one of three premium production challenges, all of which are set annually by the company’s president. The High Career Performance Bonus Plan is given to regional representatives based on their length of service, premium writings, and having qualifed for the “President’s Circle” a specific amount of times during their career. Special bonuses are also awarded to regional representatives that meet specific production goals for certain lines of business within a specified period of time.

III. MANAGEMENT AND CONTROL

Board of Directors

The board of directors consists of nine members. Three directors are elected annually to serve a three-year term. Officers are elected at the board's annual meeting. Members of the company's board of directors may also be members of other boards of directors in the holding company group. The Chairman of the Board receives $1,740 per month ($20,880 on an annualized basis) and all other board members currently receive $1,470 ($17,640 on an annualized basis) for serving on the board. All board members also receive an expense reimbursement based upon actual travel expenses incurred for meetings attended. Directors that serve on the audit committee and/or the executive compensation committee receive $525 per meeting and $475 per meeting, respectively. In addition, outside directors receive $525 per month for service on the executive committee and $475 per month for service on the investment committee. Compensation to directors for attending special board meetings is $685 per meeting. The articles of incorporation require that a majority of the board be residents of the state of Wisconsin.

Currently the board of directors consists of the following persons:

Name and Residence	Principal Occupation	Term Expires
Marsha Lindsay Madison, Wisconsin	CEO of Lindsay, Stone & Briggs, a brand marketing firm	2005
Dieter H. Nickel Merrill, Wisconsin	Chairman of the Board, former President and CEO of Church Mutual Insurance Company	2005
Wilburn J. Weber Irma, Wisconsin	Treasurer and Director of Semling-Menke Company, a door and window manufacturer	2005
Michael W. Grebe Milwaukee, Wisconsin	President and CEO of the Lynde and Harry Bradley Foundation, a private, grant making institution	2006
Michael J. Riley Laurel, Maryland	A Principal at Riley Associates, LLC, a Consulting firm serving business, government agencies and nonprofit organizations	2006
David B. Smith, Jr. Merrill, Wisconsin	Consultant and Private Investor, former Vice President of labor relations for Weyerhaeuser Company	2006

Debra Waller Winthrop Harbor, Illinois	Chairman and CEO of Jockey International Inc., an apparel manufacturer	2007
Gerald Whitburn Merrill, Wisconsin	President and CEO of Church Mutual Insurance Company	2007
Walter H. White, Jr. London, England	Partner in the law firm of White and Jones LLP	2007

Officers of the Company

The officers serving at the time of this examination are as follows:

Name	Office	2003 Compensation*
Gerald Whitburn	President and Chief Executive Officer	$528,916
Michael E. Ravn	Executive Vice President	230,354
John F. Cleary	Secretary and General Counsel	241,132
Herman W. Vandenberg	Treasurer	104,975
Randy J. Bradner	Vice President – Underwriting	172,760
Christopher A. Graham	Vice President – Chief Information Officer	183,311
Carol A. Holz	Vice President – Office Services	155,995
Russell A. Leyk	Vice President – Claims	177,737
Patrick M. Moreland	Vice President – Marketing	137,926
Timothy J. O'Leary	Vice President – Director of Group Sales	135,960
David L. Springborn	Vice President – Corporate Pricing, Products, and Line Services	156,572
Richard A. Huseby	Vice President – Human Resource and Strategic Initiatives	160,013
James P. Jordan	Vice President – Sales and Marketing	164,825
Daniel T. Vander Heiden	Vice President – Chief Financial Officer	182,038

* Note that the 2003 compensation for the executive officers do not include the company's contribution to their 401(k) retirement plan and the change in reserves for each executive's senior executive pension plan from the prior year (for those executives who qualify for the plan).

Committees of the Board

The company's bylaws allow for the formation of certain committees by the board of directors. The committees at the time of the examination are listed below:

Executive Committee
Gerald Whitburn, Chair
Dieter H. Nickel
Wiburn J. Weber
*John F. Cleary

Audit Committee
Michael J. Riley, Chair
David B. Smith, Jr.
Walter H. White, Jr.

Investment Committee
Gerald Whitburn, Chair
Dieter H. Nickel
David B. Smith, Jr.
*Daniel T. Vander Heiden

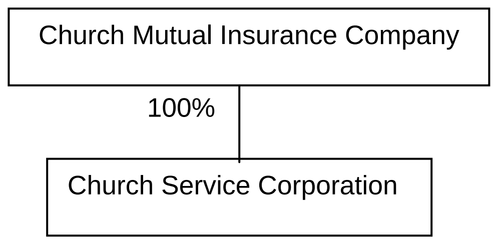
Executive Compensation Committee
Wilburn Weber, Chair
Marsha A. Lindsay
Michael W. Grebe

*Non-voting member of the committee

IV. AFFILIATED COMPANIES

Church Mutual Insurance Company is the ultimate parent of a holding company system. The organizational chart below depicts the relationships among the affiliates in the group. A brief description of the significant affiliates follows the organizational chart.

Organizational Chart
As of December 31, 2003



Church Service Corporation

Church Service Corporation (hereinafter CSC) was organized as an insurance agency in 1952 for the purpose of placing business with other insurers on lines of business, which Church Mutual was unwilling or not licensed to write such as fidelity and surety bond insurance, liquor liability insurance, and group travel accident insurance. Over the years, Church Mutual customers accommodated by CSC have been moved from CSC-brokered policies into Church Mutual products as soon as they become available. Specific examples of lines of business formerly available only through CSC brokerage, but subsequently moved into Church Mutual's expanded product line, include church automobile; umbrella; directors', officers', and trustees' insurance; systems equipment breakdown including boiler and machinery, and computer coverage. Although narrowed in scope, CSC has maintained its original purpose.

Church Mutual directly owned CSC until 1969 when the Office of the Commissioner of Insurance directed the company to divest itself of the agency. Insurance laws in effect in 1969 prohibited ownership affiliation. An agent of the company purchased the stock of the agency and subsequently sold it to directors, officers, and employees of Church Mutual. Since 1971, it has been legal for Wisconsin-domiciled insurers to form or acquire subsidiaries to perform functions or provide services that are ancillary to their insurance operations. Subsequent to the prior exam, which recommended that the company negotiate repurchase of CSC, Church Mutual repurchased the stock of CSC for $1,779,190 on January 1, 1997. This included goodwill of $449,613. Subsequently CSC paid a dividend to Church Mutual to reduce the invested securities held by CSC.

As of December 31, 2003, Church Service Corporation reported assets of $242,566, liabilities of ($46,545), and retained earnings of $289,111. Operations for 2003 produced net income before taxes of $23,153. The company reports the value of CSC on Schedule D at $435,995, which is unamortized goodwill plus stockholders equity. The unamortized goodwill Church Mutual held in CSC at December 31, 2003, was $146,884.

Agreements with Affiliates

The company was unable to provide the Office of the Commissioner of Insurance with a copy of their affiliated tax allocation agreement. Also the company has no cost allocation, service or management agreements with CSC. This will be discussed further in the Summary of Examination Results section of this report.

V. REINSURANCE

The company's reinsurance portfolio and strategy is described below. A list of the companies that have a significant amount of reinsurance in force at the time of the examination follows. The contracts contained proper insolvency provisions.

Nonaffiliated Ceding Contracts

1. Type: Property Excess of Loss

Reinsurers: General Reinsurance Corporation is a 40% Participant
Mutual Reinsurance Bureau (MRB) is a 60% Participant. In 2004, MRB is made up of three insurance companies. Each participant's share is equal to one-third of MRB's share of the risk. MRB participants are as follows:

- Auto-Owners Insurance Company
- Employers Mutual Casualty Company
- Motorists Mutual Insurance Company

In the 2003 contract year MRB consisted of the three companies noted above and Farmers Mutual Hail Insurance Company of Iowa, each of which shared one-forth of MRB's share of the risk.

Scope: Fire, Allied Lines, Property sections of multiple peril policies, Earthquake and Inland Marine

Retention:
(1) First Layer
  a) $500,000 for any one risk, each loss occurrence relating to homeowners multiple peril and dwelling fire policies
  b) $700,000 for any one risk, each loss occurrence relating to all other lines of business covered under this contract other than what was described in the previous paragraph
(2) Second Layer
  a) $1,500,000 for any one risk, each loss occurrence for all business covered under this contract
(3) Third Layer
  a) $3,000,000 for any one risk, each loss occurrence for all lines of business covered under this contract

Coverage:
(1) First Layer
  a) $1,000,000 excess of $500,000 for any one risk, each loss occurrence relating to homeowners multiple peril and dwelling fire policies
  b) $800,000 excess of $700,000 for any one risk, each loss occurrence relating to all other lines of business covered under this contract other than what was described in the previous paragraph
  c) $2,400,000 for each loss occurrence for all business (combined risk)
  d) $2,400,000 for any one and all losses arising from any one or multiple acts of terrorism or counter-terrorism
(2) Second Layer
  a) $1,500,000 excess of $1,500,000 for any one risk, each loss occurrence for all lines of business covered under this contract
  b) $4,500,000 for any one loss occurrence (combined risk)

c) $4,500,000 for any one and all losses arising from any one or multiple acts of terrorism or counter-terrorism

(3) Third Layer

a) $4,500,000 excess of $3,000,000 for any one risk, each loss occurrence for all lines of business covered under this contract
b) $9,000,000 for any one loss occurrence (combined risk)
c) $9,000,000 for any one and all losses arising from any one or multiple acts of terrorism or counter-terrorism

Premium: (1) First Layer – 4.55% of gross written premiums
(2) Second Layer – 1.50% of gross written premiums
(3) Third Layer – 0.65% of gross written premiums

One full reinstatement is permitted for no additional premium under each layer covered under this contract. A second full reinstatement is permitted for coverage under the third layer for additional premium equal to a pro rata portion of the annual premium based on the time remaining in the annual period. A third reinstatement is permitted for additional premium equal to a pro rata portion of half of the annual premium based on the time remaining in the annual period. The third reinstatement is only for 50% of the maximum ceded losses covered under the third layer.

Commissions: (1) First Layer: Contingent commission equal to 75% of the reinsurer's profit
(2) Second Layer: Contingent commission equal to 50% of the reinsurer's profit

Reinsurer's profit is calculated in the following manner:

- reinsurance premiums earned during the period; less
- paid loss and LAE during the period; less
- loss reserves for outstanding claims that occurred during the period; less
- an estimate for IBNR claims; less
- the reinsurer's home office expense for the period (15% and 25% of the reinsurance premiums earned during the period for the First and Second Layers respectively); less
- any deficit pulled forward from prior periods

Effective date: April 1, 2004, and is continuous

Termination: By either party giving not less than 90 days' written notice as of any March 31st. The reinsurers shall not be liable for losses discovered after the effective date of termination.

2. Type: Obligatory First Surplus – Pro Rata

Reinsurers: SCOR Reinsurance Company (40%)
Mutual Reinsurance Bureau (60%)

Scope: Fire, Allied Lines, Property sections of multiple peril policies, Earthquake and Inland Marine

Retention: $1,500,000 for any one risk, each loss occurrence for all business covered under this contract

Coverage: This agreement provides coverage for losses and loss adjustment expenses as follows:

(1) Institutional business: $4,500,000, for any one risk
(2) Institutional business: $6,000,000, for any one risk
(3) Other than institutional business: $1,500,000, for any one risk
(4) $20,000,000 as respects any one loss occurrence

There is a loss corridor deductible provision included in this agreement as follows: If the loss ratio incurred for the block of business ceded for any one period is between 66% and 80%, the company would retain losses equal to the difference between the actual loss ratio and 66% multiplied by earned premium for the period.

Premium: The reinsurer's surplus share of subject net written premium

Commissions: 28% of subject net written premiums

Effective date: April 1, 2003, and was terminated August 1, 2003.

Note: This contract was included in the outline of current reinsurance coverage because the company writes three-year policies and therefore any policies that had effective dates prior to August 1, 2003, would still be covered under this contract.

Termination: By either party giving not less than 90 days' written notice

3. Type: Semi-Automatic Facultative Excess of Loss

Reinsurers: Everest Reinsurance Company

Scope: Commercial property business

Retention: Established per individual risk

Coverage: Cessions made shall not exceed the company's net and treaty retention on any one risk, subject to a maximum cession on any one risk, per occurrence of:

- Frame construction classes and property of other construction classes located under ISO fire protection classes 9 and 10: $4,000,000
- Joisted masonry and Noncombustible construction classes located under ISO fire protection classes 1 through 8: $6,000,000
- Masonry noncombustible, Semi-fire resistive and Fire resistive construction classes located under ISO fire protection classes 5 through 8: $6,000,000
- Masonry noncombustible, Semi-fire resistive and Fire resistive construction classes located under ISO fire protection classes 1 through 4: $7,500,000

The company is to notify the reinsurer for acceptance of coverage for ceded reinsurance risks of $10,000,000 or greater. If accepted the coverage for these risks are $15,000,000 per loss, per occurrence

Premium: Established per individual risk based on the type of risk and amount of risk being ceded

Commissions: None

Effective date: August 1, 2003, and is continuous

Termination: By either party giving not less than 120 days' written notice of the termination effective date. The reinsurer shall remain liable for policies in force on the effective date of termination until expiration or cancellation of the said polices, but in no event shall the reinsurer's liability go beyond thirty-six months following the termination date of this agreement.

4. Type: First Catastrophe Excess of loss

Reinsurer: Mutual Reinsurance Bureau

Scope: Habitational risks in the Wisconsin counties of Lincoln and Marathon for the following property lines of business: Fire, Allied Lines, Property sections of homeowners multiple peril policies, Earthquake, and Inland Marine

Retention: $2,000,000 per loss occurrence for any one period

Coverage: $3,000,000 excess of $2,000,000 per loss occurrence and $6,000,000 with respect to aggregate losses in a period (April 1 to March 31 or a full year)

Premium: Flat annual premium of $39,000

One full reinstatement is permitted for additional premium equal to a pro rata portion of the annual premium based on the time remaining in the annual period

Commissions: None

Effective date: April 1, 2004, and is continuous

Termination: By either party giving not less than 90 days' written notice as of any March 31st. The reinsurers shall not be liable for losses discovered after the effective date of termination.

5. Type: First Property Catastrophe Excess of loss

Reinsurer: Mutual Reinsurance Bureau

Scope: Fire, Allied Lines, Property sections of multiple peril policies, Earthquake and Inland Marine

Retention: $7,500,000 with respect to the first loss occurrence for any one period

$5,000,000 with respect to the second and all subsequent loss occurrences for any one period

Coverage:	$5,000,000 excess of $7,500,000 with respect to the first loss occurrence $5,000,000 excess of $5,000,000 with respect to the second all subsequent loss occurrences for any one period $10,000,000 with respect to aggregate losses in a period (April 1 to March 31 or a full year)
Premium:	Flat annual premium of $1,100,000 One full reinstatement is permitted for additional premium equal to a pro rata portion of flat annual premium based on the time remaining in the annual period
Commissions:	Contingent commission equal to 100% of the reinsurer's profit Reinsurer's profit is calculated in the following manner: - reinsurance premiums earned during the period; less - paid losses during the period; less - the reinsurer's expense for the period (10% of the reinsurance premiums earned during the period)
Effective date:	April 1, 2004, through March 31, 2006
Termination:	By either party giving not less than 90 days' written notice as of any March 31st. The reinsurers shall not be liable for losses discovered after the effective date of termination.

6. Type: Property Catastrophe Excess of loss

Reinsurers:

	Participating Percentage			
Reinsurer	**Second Layer**	**Third Layer**	**Fourth Layer**	**Fifth Layer**
American Agricultural Insurance Company	5.00%	5.50%	4.50%	2.00%
Converium Limited	2.43	2.50	2.29	1.85
Country Mutual Insurance Company	1.50	1.00		
Employers Mutual Casualty Company		2.00		
Endurance Specialty Insurance Ltd.	2.00	3.50	5.00	3.00
Folksamerica Reinsurance Company		3.50	3.00	3.00
Hannover Re (Bermuda) Ltd.		5.50	5.00	3.00
Lloyd's Underwriters	74.70	56.33	61.40	67.96
Mapfre Reinsurance Corporation	1.50	1.50	1.00	2.00
Odyssey America Reinsurance	4.87	4.17	3.81	3.69
Odyssey America Reinsurance Corporation			2.50	3.00
QBE Reinsurance Corporation			2.50	2.00
Transatlantic Reinsurance Company	8.00	8.50	5.50	6.50
XL Re Limited		6.00	3.50	2.00

Scope: Property business including Automobile Physical Damage

Retention:	Second Layer –	$12,500,000 per loss occurrence plus 5% of each loss not to exceed $375,000
	Third Layer –	$20,000,000 per loss occurrence plus 5% of each loss not to exceed $750,000
	Fourth Layer –	$35,000,000 per loss occurrence plus 5% of each loss not to exceed $750,000
	Fifth Layer –	$50,000,000 per loss occurrence plus 5% of each loss not to exceed $1,250,000
Coverage:	Second Layer –	95% of $7,500,000 excess of $12,500,000 per loss occurrence
	Third Layer –	95% of $15,000,000 excess of $20,000,000 per loss occurrence
	Fourth Layer –	95% of $15,000,000 excess of $35,000,000 per loss occurrence
	Fifth Layer –	95% of $25,000,000 excess of $50,000,000 per loss occurrence

One full reinstatement for each layer is permitted for additional premium equal to a pro rata portion of the annual premium for each layer

Premium:	Second Layer –	0.575% of net direct written premium, minimum premium equaling $969,000
	Third Layer –	0.6252% of net direct written premium, minimum premium equaling $1,100,000
	Fourth Layer –	0.4390% of net direct written premium, minimum premium equaling $741,000
	Fifth Layer –	0.4620% of net direct written premium, minimum premium equaling $779,000

Commissions: None

Effective date: April 1, 2004

Termination: April 1, 2005

7. Type: Casualty Excess of Loss

Reinsurers:

	Participation		
Reinsurer	**First Layer**	**Second Layer**	**Third Layer**
Through Mutual Reinsurance Bureau			
- Auto-Owners Insurance Company	33.33%	1.67%	1.67%
- Employers Mutual Casualty Company	33.33	1.66	1.66
- Motorists Mutual Insurance Company	33.33	1.67	1.67
Through Aon Limited			
- Aspen Insurance UK Limited		25.00	17.10
- Lloyd's Underwriters		28.00	35.90
Folksamerica Reinsurance Company		25.00	25.00
Hannover Ruckversicherungs-Aktiengesellschaft		17.00	17.00
	100.00%	100.00%	100.00%

Scope: Casualty sections of multiple peril policies, automobile liability, and general bodily injury liability including personal liability, general liability, worker's compensation and employers liability, medical payments, professional liability, and employee benefits liability

Retention:
(1) First Layer – $1,000,000 per loss occurrence
(2) Second Layer – $3,000,000 per loss occurrence
(3) Third Layer – $10,000,000 per loss occurrence

Coverage:
(1) First Layer
 a) $2,000,000 excess of $1,000,000 per loss occurrence
 b) $6,000,000 for any one and all losses arising from any one or multiple acts of terrorism or counter-terrorism
(2) Second Layer
 a) $7,000,000 excess of $3,000,000 per loss occurrence
 b) One full reinstatement, pro rata as to amount and 100% as to time
(3) Third Layer
 a) $10,000,000 excess of $10,000,000 per loss occurrence
 b) One full reinstatement, pro rata as to amount and 100% as to time

Premium:
(1) First Layer – 4.5% of net written premium
(2) Second Layer – 0.32% of net written premium, minimum premium equaling $670,000
(3) Third Layer – 0.21% of net written premium, minimum premium equaling $440,000

Commissions: Contingent commission equal to 75% of the reinsurer's profit and only pertains to the First Layer of coverage

Reinsurer's profit is calculated in the following manner:
- reinsurance premiums earned during the period; less
- paid losses and LAE during the period; less
- the reinsurer's expense for the period (15% of the reinsurance premiums earned during the period)
- any deficit pulled forward from prior periods (only applies to the first layer calculation)

Effective date: April 1, 2004, and is continuous

Termination: By either party giving not less than 90 days' written notice as of any March 31st. The reinsurers shall not be liable for losses discovered after the effective date of termination.

8. Type: Commercial Umbrella Quota Share and Excess of Loss

Reinsurer: General Reinsurance Corporation

Scope: All commercial umbrella business

Retention: 50% of the first $1,000,000 per occurrence and 5% of the next $4,000,000 per occurrence

Coverage: 50% of the first $1,000,000 per occurrence, 95% of the next $4,000,000 per occurrence, and 100% of the next $5,000,000 per occurrence

Premium:
a) 50% of the written premium charged for policy limits up to and including $1,000,000
b) 95% of the written premium for policy limits in excess of $1,000,000, up to and including $5,000,000
c) 100% of written premium for policy limits in excess of $5,000,000, up to and including $10,000,000

Commissions: 32.5% of written premium noted in parts a) and b) of the premium section and 25% of written premium for long term care facilities and written premium noted in part c of the premium section

The company also has a contingent commission based on 50% of the amount by which the reinsurer's income exceeds the reinsurer's outgo for each contingent period

Effective date: July 1, 2002, and is continuous

Termination: By either party giving not less than 90 days' written notice of the termination effective date. The reinsurer shall remain liable for policies in force on the effective date of termination until expiration or cancellation of the said polices, but in no event shall the reinsurer's liability go beyond one year following the termination date of this agreement.

9. Type: Quota Share

Reinsurer: Swiss Reinsurance Company

Scope: All business written by the company

Retention: 90% of the aggregate net and unreinsured losses

Coverage: 10% of the aggregate net retained liability by the company, on a paid basis

Premium: 10% of net written premium and a reinsurance margin of 4.4% of subject net earned premium (hereinafter SNEP). The company is also subject to maintenance fees equal to 0.5% of SNEP commencing April 1, 2005, 0.6% of SNEP commencing April 1, 2006, and 1.2% of SNEP for each additional twelve month period

Commissions: 26% of net written premium and 31% of net written premium if the company's net loss ratio is 83% or higher

Commutation: Unilaterial right to commute – any calendar quarter end if the net funds held account balance equals or exceeds the net unpaid ceded ultimate net loss balance, which includes IBNR; or for a commutation amount equal to the funds held account balance at the date of commutuation.

Reinsurer's consent to commute – any calendar quarter end on or after the termination of the agreement to commute all ceded ultimate net losses outstainding hereunder for an amount mutually agreed upon.

The funds held account is to be established and maintained by the company and is comprised of the following cumulative amounts:

(1) The first quarter subject net unearned premium; plus
(2) Reinsurance premium credited each quarter thereafter; less
(3) Reinsurer's margin each quarter; less
(4) Maintenance fee; less
(5) Ceding commissions paid by the reinsurer each quarter; less
(6) Ceded ultimate net losses paid by the reinsurer each quarter, plus
(7) Interest credit of 1.125% credited quarterly

Effective date: October 1, 2003

Termination: October 1, 2004

Nonaffiliated Assuming Contract

1. Type: Catastrophe Pool Reinsurance Agreement

Reinsured: Mutual Reinsurance Bureau

Scope: Aggregate and catastrophe excess contracts, or similar covers

Retention and Limit: 3% of Mutual Reinsurance Bureau's net retained liability, not to exceed a maximum of $7,500,000 for any one Original Reassured on any one occurrence. (MRB's net retained liability on Original Agreements pertaining to one Original Reassured will not exceed $10,000,000 any one occurrence basis or $7,500,000 in the aggregate on any one agreement year when the original agreement is written on an aggregate basis)

Premium: Proportionate share of premiums on each Original Agreement

Commissions: 7.5% on all original ceded premiums and contingent commissions equal to 15% of the pool's earned premium

The pool's profit is calculated in the following manner:

- reinsurance premiums earned during the period; less
- paid loss and LAE during the period; less
- home office expense for the period (20% of the reinsurance premiums earned during the period); less
- any deficit pulled forward from prior periods

Effective date: January 1, 2004, and is continuous

Termination: By either party giving not less than 90 days' written notice as of any December 31st. The reinsurer shall not be liable for any loss activity after the effective date of the termination agreement.

VI. FINANCIAL DATA

The following financial statements reflect the financial condition of the company as reported to the Commissioner of Insurance in the December 31, 2003, annual statement. Also included in this section are schedules that reflect the growth of the company, NAIC Insurance Regulatory Information System (IRIS) ratio results for the period under examination, and the compulsory and security surplus calculation. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Surplus per Examination."

Church Mutual Insurance Company
Assets
As of December 31, 2003

	Assets	Nonadmitted Assets	Net Admitted Assets
Bonds	$502,060,569	$ 0	$502,060,569
Stocks:			
Preferred stocks	2,088,000	0	2,012,000
Common stocks	50,599,819	0	50,599,819
Occupied by the company	3,362,550	0	3,362,550
Cash	1,956,144	0	1,956,145
Short-term investments	22,771,814	0	22,771,814
Receivable for securities	6,501,234	0	6,501,234
Write-ins for invested assets:			
Cash surrender value of life insurance	9,747,963	0	9,747,963
Investment income due and accrued	6,224,246	0	6,224,246
Premiums and considerations:			
Uncollected premiums and agents' balances in course of collection	43,751,272	1,776,811	41,974,462
Deferred premiums, agents' balances, and installments booked but deferred and not yet due	57,890,501	0	57,890,501
Reinsurance:			
Amounts recoverable from reinsurers	2,731,133	0	2,731,133
Net deferred tax asset	21,700,000	0	21,700,000
Guaranty funds receivable or on deposit	944,574	0	944,574
Electronic data processing equipment and software	1,438,903	0	1,438,903
Furniture and equipment, including health care delivery assets	1,487,588	1,487,588	0
Write-ins for other than invested assets:			
Security deposit on leased equipment	1,794	0	1,794
Goodwill	1,013,690	0	1,013,690
Equities in pools and associations	2,699,405	0	2,699,405
Total Assets	$738,971,201	$3,264,399	$735,706,803

Church Mutual Insurance Company
Liabilities, Surplus, and Other Funds
As of December 31, 2003

Losses		$198,463,568
Reinsurance payable on paid loss and loss adjustment expenses		690,238
Loss adjustment expenses		74,484,000
Commissions payable, contingent commissions, and other similar charges		(1,425,641)
Other expenses (excluding taxes, licenses, and fees)		9,015,512
Taxes, licenses, and fees (excluding federal and foreign income taxes)		5,484,990
Current federal and foreign income taxes		10,538,203
Net deferred tax liability		3,300,000
Borrowed money and interest thereon		306,531
Unearned premiums		163,217,918
Advance premium		3,717,161
Dividends declared and unpaid:		
Policyholders		5,730,000
Ceded reinsurance premiums payable (net of ceding commissions)		10,993,934
Funds held by company under reinsurance treaties		19,082,890
Amounts withheld or retained by company for account of others		1,210,768
Provision for reinsurance		250,149
Payable for securities		12,258,397
Write-ins for liabilities:		
Reserve for pensions and deferred compensation		11,419,618
Reserve for post retirement benefits		1,799,926
Total Liabilities		530,538,161
Write-ins for special surplus funds:		
Guarantee fund	$ 1,600,000	
Unassigned funds (surplus)	203,568,642	
Surplus as Regards Policyholders		205,168,642
Total Liabilities and Surplus		$ 735,706,803

Church Mutual Insurance Company
Summary of Operations
For the Year 2003

Underwriting Income		
Premiums earned		$298,740,002
Deductions:		
Losses incurred	$189,931,799	
Loss expenses incurred	34,467,285	
Other underwriting expenses incurred	67,055,406	
Total underwriting deductions		291,454,490
Net underwriting gain or (loss)		7,285,512
Investment Income		
Net investment income earned	21,651,391	
Net realized capital gains or (losses)	4,000,487	
Net investment gain or (loss)		25,651,877
Other Income		
Net gain or (loss) from agents' or premium balances charged off	(220,782)	
Finance and service charges not included in premiums	1,194,346	
Write-ins for miscellaneous income:		
Miscellaneous	26,213	
Interest on borrowed money	(31,945)	
Amortization of goodwill	(506,845)	
Total other income		460,986
Net income (loss) before dividends to policyholders and before federal and foreign income taxes		33,398,376
Dividends to policyholders		3,879,342
Net income (loss) after dividends to policyholders but before federal and foreign income taxes		29,519,034
Federal and foreign income taxes incurred		11,500,000
Net Income		$ 18,019,034

Church Mutual Insurance Company
Cash Flow
For the Year 2003

Premiums collected net of reinsurance			$298,494,745
Net investment income			23,484,415
Miscellaneous income			17,678,075
Total			339,657,235
Benefit and loss related payments		$194,253,584	
Commissions, expenses paid, and aggregate write-ins for deductions		65,842,427	
Dividends paid to policyholders		2,199,342	
Federal and foreign income taxes paid (recovered)		7,419,362	
Total deductions			269,714,715
Net cash from operations			69,942,520
Proceeds from investments sold, matured, or repaid:			
Bonds	$159,923,412		
Stocks	11,098,681		
Total investment proceeds		171,022,093	
Cost of investments acquired (long-term only):			
Bonds	236,003,451		
Stocks	11,154,579		
Real estate	(5,175)		
Miscellaneous applications	1,324,160		
Total investments acquired		248,477,015	
Net cash from investments			(77,454,922)
Cash from financing and miscellaneous sources:			
Borrowed funds received		(23,495)	
Other cash provided (applied)		4,999,389	
Net cash from financing and miscellaneous sources			4,975,894
Reconciliation			
Net change in cash and short-term investments			(2,536,508)
Cash and short-term investments, December 31, 2002			27,264,466
Cash and short-term investments, December 31, 2003			$ 24,727,958

Church Mutual Insurance Company
Compulsory and Security Surplus Calculation
December 31, 2003

Assets		$735,706,803
Less security surplus of insurance subsidiaries		0
Less liabilities		530,538,161
Adjusted surplus		205,168,642
Annual premium:		
Lines other than accident and health	$313,907,521	
Factor	20%	
Compulsory surplus (subject to a minimum of $2 million)		62,781,504
Compulsory surplus excess (or deficit)		$142,387,138
Adjusted surplus (from above)		$205,168,642
Security surplus: (140% of compulsory surplus, factor reduced 1% for each $33 million in premium written in excess of $10 million, with a minimum factor of 110%)		82,243,770
Security surplus excess (or deficit)		$122,924,872

Church Mutual Insurance Company
Reconciliation and Analysis of Surplus
For the Five-Year Period Ending December 31, 2003

The following schedule is a reconciliation of total surplus during the period under examination as reported by the company in its filed annual statements:

	2003	2002	2001	2000	1999
Surplus, beginning of year	$172,173,019	$169,817,914	$161,028,320	$151,559,005	$131,312,107
Net income	18,019,034	11,006,984	6,209,770	14,786,052	15,287,612
Net unrealized capital gains or (losses)	12,609,375	(11,303,457)	(8,923,036)	(6,684,018)	3,821,577
Change in net deferred income tax	2,400,000	3,400,000	1,100,000	0	0
Change in non-admitted assets	217,362	(769,643)	(355)	88,387	265,814
Change in provision for reinsurance	(250,149)	21,221	25,347	(23,163)	(6,224)
Cumulative effect of changes in accounting principles	0	0	10,377,869	0	0
Change in excess of statutory reserves over statement reserves	0	0	0	1,302,057	878,119
Surplus, end of year	$205,168,642	$172,173,019	$169,817,914	$161,028,320	$151,559,005

Church Mutual Insurance Company
Insurance Regulatory Information System
For the Five-Year Period Ending December 31, 2003

The company's NAIC Insurance Regulatory Information System (IRIS) results for the period under examination are summarized below. Unusual IRIS results are denoted with asterisks and discussed below the table.

	Ratio	2003	2002	2001	2000	1999
#1	Gross Premium to Surplus	216%	208%	169%	162%	164%
#2	Net Premium to Surplus	155	162	133	129	130
#3	Change in Net Writings	14	23	9	5	2
#4	Surplus Aid to Surplus	5	4	3	2	3
#5	Two-Year Overall Operating Ratio	91	94	94	90	92
#6	Investment Yield	4.0*	4.9	5.3	5.5	5.1
#7	Change in Surplus	16	3	5	7	14
#8	Liabilities to Liquid Assets	80	78	74	71	73
#9	Agents' Balances to Surplus	20	16	8	13	12
#10	One-Year Reserve Development to Surplus	(11)	0	(5)	(9)	(7)
#11	Two-Year Reserve Development to Surplus	(8)	1	(14)	(13)	(15)
#12	Estimated Current Reserve Deficiency to Surplus	2	5	(18)	(16)	(14)

Ratio #6 had an unusual ratio for 2003. This ratio measures the amount of the company's net investment income as a percentage of the average amount of cash and invested assets. In 2003, the company's net investment income earned decreased 6.7% to $21.7 million and realized capital gains decreased 13% from the prior year to $4 million in spite of an increase in invested assets of 18.9%. Those results combined with the reinvestment of proceeds from the disposal of invested assets into bonds with low interest rates caused investment yield to decrease in 2003, and were the primary factors attributable towards the exceptional result in 2003.

Growth of Church Mutual Insurance Company

Year	Admitted Assets	Liabilities	Surplus As Regards Policyholders	Net Income
2003	$735,706,803	$530,538,161	$205,168,642	$18,019,034
2002	611,276,818	439,103,799	172,173,019	11,006,984
2001	544,244,238	374,426,324	169,817,914	6,209,770
2000	496,442,382	335,414,062	161,028,320	14,786,052
1999	472,719,217	321,160,212	151,559,005	15,287,612
1998	439,497,276	308,185,169	131,312,107	11,930,349

Year	Gross Premium Written	Net Premium Written	Premium Earned	Loss And LAE Ratio	Expense Ratio	Combined Ratio
2003	$443,786,925	$317,786,863	$298,740,002	75.1%	21.0%	96.1%
2002	358,785,856	278,967,136	250,774,890	76.6	23.5	100.1
2001	286,595,585	226,177,787	217,154,667	82.2	25.1	107.3
2000	261,525,458	207,302,769	201,252,920	74.1	26.7	100.8
1999	249,044,708	197,629,421	195,675,547	74.5	25.7	100.2
1998	242,324,303	193,767,197	191,766,015	76.0	25.3	101.3

The company has experienced surplus growth over the past five years of 56%, while at the same time maintaining a conservative premiums written to surplus ratio. Premium growth has been steady over the five-year period under examination and is attributable to the company's successful marketing strategy as well as the addition of new products and the enhancement of products already offered. The company has reduced its expense ratio and maintained a stable loss ratio over the five-year period, thus contributing to a positive net income for each year under examination. 2001 was the only year the company experienced net income lower than $10 million, which was mainly attributable to large windstorms that occurred during the spring of that year and resulted in a net loss and LAE ratio of 82.2%.

Reconciliation of Surplus per Examination

No adjustments were made to surplus as a result of the examination. The amount of surplus reported by the company as of December 31, 2003, is accepted.

Examination Reclassifications

	Debit	Credit
Net Deferred Tax Liability	$3,300,000	$
Net Deferred Tax Asset		3,300,000
Other Expenses Payable	129,631	
Other Amounts Receivable Under Reinsurance Contracts	2,249,490	
Ceded Reinsurance Premiums Payable	149,613	
Commissions Payable, Contingent Commissions and Other Similar Charges		2,528,734
Total reclassifications	$5,828,734	$5,828,734

VII. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

There were four specific comments and recommendations in the previous examination report. Comments and recommendations contained in the last examination report and actions taken by the company are as follows:

1. Invested Assets—It is recommended that the company list securities receivable on the "Receivable for securities" line of the balance sheet per the Annual Statement Instructions – Property and Casualty.

   Action—Compliance

2. Advance Premium—It is recommended that on future annual statements the company report advance premium as an addition to the unearned premium reserve or as a separate write-in on the balance sheet labeled "Advance Premium" instead of netting the advance premiums against premium receivable.

   Action—Compliance

3. Loss and LAE Reserves, Excess of Statutory Reserves over Statement Reserves—It is suggested that the company direct its actuarial consultants to include an evaluation of loss adjusting expense under both the old ALAE/ULAE and the new DCC/AO definitions until there is sufficient data under the new definition to promote meaningful actuarial analysis.

   Action—Compliance

4. Loss and LAE Reserves, Excess of Statutory Reserves over Statement Reserves—It is suggested that the company annually maintain permanent documentation of events and actuarial assumptions that may affect analysis of reserves.

   Action—Compliance

Summary of Current Examination Results

Executive Compensation

The liability balances reported on the company’s balance sheet relating to executive compensation were accurate and complete; however, the executive compensation information reported in the Annual Statement supplemental filing to OCI did not include the company's contribution towards their executives' 40l(k) plan as well as the change in reserves for their executives’ supplemental executive retirement plan (SERP). According to s. 611.63 (4), Wis. Stat., companies are to report to the Commissioner, on an annual basis, all direct and indirect remuneration for services, including retirement and other deferred compensation benefits and stock options, paid or accrued each year for the benefit of each director and each officer and employee whose remuneration exceeds the amount established by the Commissioner. Therefore, it is recommended that the company report all remuneration to executives, which includes deferred compensation and other retirement compensation plans sponsored by the company, for those executives whose remuneration meets the requirements to be reported to the Commissioner of Insurance in accordance with s. 611.63 (4), Wis. Stat.

Business Information Security

Access to the company’s computer resources should be limited to the rights required for the individual needs of the employees to perform the duties outlined in their job descriptions. The company does have in place a formalized procedure to limit access to computer resources based upon security codes built into the User ID of employees and applies this process at the time of hire and when the employee takes on new job responsibilities. Although an informal procedure exists, the company should have a formalized procedure to periodically review access rights to verify rights remain commensurate to users’ needs and to detect and remove obsolete IDs. It is recommended that the company institute a formalized procedure to review access rights on a scheduled periodic basis.

The examiners noted that the company was in the beginning stages of centralizing existing security policies and adding new policies into a comprehensive security policy. By centralizing these formal policies into a comprehensive manual the assignment of responsibilities and basic rules, guidelines, and definitions for personnel provide quick access within the organization as to how the company's critical computer assets, including electronic data and proprietary information, are secured. This helps prevent inconsistencies in the application of security procedures that may introduce risks to critical computer resources. It is recommended that the company centralize existing security policies and implement a broader written security policy that introduces security measures that protect its critical computer assets.

Holding Company

The company made an original holding company registration statement filing with this office on January 28, 1991, to report its wholly owned affiliate Church Service Corporation. However, the company has not made a holding company registration statement filing since. According to s. Ins 40.03 (2), Wis. Adm. Code, holding company registration statement filings are to be made annually. Therefore it is recommended that the company makes annual Holding Company Registration Statement filings in accordance with s. Ins 40.03 (2), Wis. Adm. Code.

According to the company's notes to the financial statement and CPA Audit Report, the company joins its subsidiary (Church Service Corporation) in the filing of a consolidated federal income tax return and is party to a federal income tax allocation agreement. The examiner requested this agreement; however, no copy was ever provided by the company. It was also discovered that the company does not have a formal written cost-sharing agreement with its affiliate (CSC) in regards to sharing the company's home office space, employees, and supplies. Currently the company has an informal budget and cost allocation process that allocates a reasonable amount of costs (home office and employee expenses) to CSC. Having an affiliated cost-sharing agreement would address problems that may arise due to the misallocation of expenses amongst affiliates. It is recommended that the company create, and file with this office for approval, an affiliated tax allocation agreement and an affiliated cost-sharing agreement with Church Service Corporation.

The examiner reviewed the valuation method the company used to report their wholly owned subsidiary CSC at year-end. The company is currently using the statutory equity method as directed by this office in 1998. However, since that time the NAIC has adopted a comprehensive accounting guidance effective in 2001, which provides slightly different accounting guidance on the valuation of subsidiaries. According to Statement of Statutory Accounting Principles (SSAP) 46, paragraph 7, part b, sub paragraph iii, investments in non-insurance subsidiaries that have significant ongoing operations beyond the holding of assets that are primarily for the direct or indirect benefit or use of the reporting entity shall be recorded based on the audited GAAP equity of the investee. As described in the "Affiliated Companies" section of the report CSC does have significant ongoing operations and therefore is required to be audited annually in order for CMIC to record it as an admitted asset on the Annual Statement. No adjustment to surplus will be made in regards to this finding due to the aggregate adjustments to surplus for the examination were well below tolerable error set for this examination and therefore wouldn't materially affect the company's reported surplus. However, it is recommended that the company value its subsidiary in accordance with the NAIC Accounting Practices and Procedures Manual.

Other Amounts Receivable Under Reinsurance Contracts $2,249,490

As a result of the examination, the above balance was increased from a zero balance to $2,249,490 as a result of the reclassification described subsequently under the heading, "Commissions Payable, Contingent Commissions and Other Similar Charges."

Net Deferred Tax Asset $18,400,000

The original asset of $21,700,000 represents the expected future tax consequences of temporary differences generated by statutory accounting. The net deferred tax asset calculation was reviewed and the examiners identified that the balances for Deferred Tax Assets and Deferred Tax Liabilities were presented separately on the Annual Statement, and were not offset. Reporting deferred tax assets and deferred tax liabilities separately does not agree with Statement of Statutory Accounting Principles (SSAP) 10, paragraph 7, which states that deferred tax balances shall be offset and presented as a single amount on the balance sheet. The deferred tax asset of $21,700,000 reported at year-end exceeded the deferred tax liability of $3,300,000 reported on the balance sheet, which would have resulted in the reporting of a net deferred tax asset balance of $18,400,000. A reclassification of $3,300,000 has been reflected in

Section V of this report under the heading, “Examination Reclassifications” due to this finding. It is recommended that the company report net deferred tax assets or net deferred tax liabilities as one account on the annual statement in order to comply with SSAP No. 10 of the NAIC Accounting Practices and Procedures Manual.

Review of the company’s deferred tax asset calculation also found that the nonadmitted portion of the deferred tax asset was not included in the filed annual statement in column 1 of the assets page, and was not reported as nonadmitted in column 2 of that page, and the nonadmitted portion was not disclosed in the gains and losses in surplus schedule on page 4. The net admitted portion of the asset is not affected by this nondisclosure so an adjustment to surplus was not necessary. However, it is recommended that the company disclose the nonadmitted portion of the deferred tax asset calculation in future annual statement filings in accordance with the NAIC Annual Statement Instructions-Property & Casualty and Statement of Statutory Accounting Principle No. 10 in the NAIC Accounting Practices and Procedures Manual.

Commissions Payable, Contingent Commissions and Other Similar Charges $1,103,093

The above balance represents an increase of $2,528,734 from the balance reported by the company as of December 31, 2003, due to three reclassifications, which are reflected in Section V of this report under the heading, “Examination Reclassifications.”

After reviewing the commissions payable detail, it was discovered that the company netted commissions receivable of $149,613 and contingent commissions receivable of $2,249,490 against the commissions payable balance. According to the NAIC Annual Statement Instructions-Property and Casualty, companies are required to net the commissions receivable balance on reinsurance ceded business against ceded reinsurance premiums payable. Companies are also required to report contingent commissions receivable on the balance sheet line titled “Other amounts receivable under reinsurance.” A reclassification of $2,399,103 has been made in regards to this finding. It is recommended that the company properly report ceded commissions receivable as an offset to ceded reinsurance premiums payable in accordance with the NAIC Annual Statement Instructions-Property and Casualty and Statement of Statutory Accounting Principles No. 62, paragraph 50, in the NAIC Accounting Practices and Procedures

Manual. It is further recommended that the company properly report contingent commissions receivable on the "Other amounts receivable under reinsurance" line of the balance sheet in accordance with the NAIC Annual Statement Instructions-Property and Casualty.

It was also discovered that the company mistakenly included a portion of the independent agents' commissions payable balance in the amount of $129,631 as a component of the Other Expenses liability balance instead of reporting them on the Commissions Payable line of the balance sheet. A reclassification of $129,631 has been made in the "Reconciliation of Surplus per Examination" section of this report to reflect this finding. It is recommended that the company properly record commissions payable to their independent agents in accordance with the NAIC Annual Statement Instructions-Property and Casualty.

Other Expenses **$8,885,881**

As a result of the examination, the above balance was decreased from $9,015,512 to $8,885,881 as a result of two reclassifications described previously under the heading, "Commissions Payable, Contingent Commissions and Other Similar Charges."

Net Deferred Tax Liability **$0**

As a result of the examination, the above balance was decreased from $306,531 to $0 as a result of the reclassification described previously under the heading, "Net Deferred Tax Asset."

Ceded Reinsurance Premiums Payable **$10,844,321**

As a result of the examination, the above balance was decreased from $10,993,934 to $10,844,321 as a result of the reclassification described above under the heading, "Commissions Payable, Contingent Commissions and Other Similar Charges."

VIII. CONCLUSION

Policyholders' surplus has increased from $131,312,107 as of year-end 1998, to $205,168,642 as of year-end 2003. This represents an increase of 56% during the period under examination, which is partially attributable to steady premium growth, reduction of its expense ratio and maintaining a stable loss ratio during this time.

The examination of Church Mutual Insurance Company resulted in ten recommendations none of which were repeat recommendations, no adjustment to surplus and five reclassifications. This has been the first examination of the company since the adoption of comprehensive accounting guidance by the NAIC (effective 2001). A number of the examination findings are a result of reporting changes brought upon property and casualty insurers through the adoption of comprehensive accounting guidance. Three of the recommendations relate to their wholly owned subsidiary, Church Service Corporation, where it was discovered that a holding company filing has not been made annually to the State of Wisconsin by CMIC, the affiliate has been reported incorrectly on their annual and quarterly statement filings, and that there are no formal written cost-sharing agreements and tax-sharing agreements between the affiliates for services provided. The other recommendations pertain to statutory reporting requirements, proper annual statement filing requirements relating to executive compensation, and business information security issues.

IX. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 31 - Executive Compensation—It is recommended that the company report all remuneration to executives, which includes deferred compensation and other retirement compensation plans sponsored by the company, for those executives whose remuneration meets the requirements to be reported to the Commissioner of Insurance in accordance with s. 611.63 (4), Wis. Stat.

2. Page 31 - Business Information Security—It is recommended that the company institute a formalized procedure to review access rights on a scheduled periodic basis.

3. Page 32 - Business Information Security—It is recommended that the company centralize existing security policies and implement a broader written security policy that introduces security measures that protect its critical computer assets.

4. Page 32 - Holding Company—It is recommended that the company makes annual Holding Company Registration Statement filings in accordance with s. Ins 40.03 (2), Wis. Adm. Code.

5. Page 32 - Holding Company—It is recommended that the company create, and file with this office for approval, an affiliated tax allocation agreement and an affiliated cost-sharing agreement with Church Service Corporation.

6. Page 33 - Holding Company—It is recommended that the company value its subsidiary in accordance with the NAIC Accounting Practices and Procedures Manual.

7. Page 34 - Net Deferred Tax Asset—It is recommended that the company report net deferred tax assets or net deferred tax liabilities as one account on the annual statement in order to comply with SSAP No. 10 of the NAIC Accounting Practices and Procedures Manual.

8. Page 34 - Net Deferred Tax Asset—It is recommended that the company disclose the nonadmitted portion of the deferred tax asset calculation in future annual statement filings in accordance with the NAIC Annual Statement Instructions-Property & Casualty and Statement of Statutory Accounting Principle No. 10 in the NAIC Accounting Practices and Procedures Manual.

9. Page 34 - Commissions Payable, Contingent Commissions and Other Similar Charges—It is recommended that the company properly report ceded commissions receivable as an offset to ceded reinsurance premiums payable in accordance with the NAIC Annual Statement Instructions-Property and Casualty and Statement of Statutory Accounting Principles No. 62, paragraph 50, in the NAIC Accounting Practices and Procedures Manual. It is further recommended that the company properly report contingent commissions receivable on the "Other amounts receivable under reinsurance" line of the balance sheet in accordance with the NAIC Annual Statement Instructions-Property and Casualty.

10. Page 35 - Commissions Payable, Contingent Commissions and Other Similar Charges—It is recommended that the company properly record commissions payable to their independent agents in accordance with the NAIC Annual Statement Instructions-Property and Casualty.

X. ACKNOWLEDGMENT

The courtesy and cooperation extended during the course of the examination by the officers and employees of the company are acknowledged.

In addition to the undersigned, the following representatives of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination:

Name	Title
Jerry C. DeArmond	Insurance Financial Examiner Advanced Loss Reserve Specialist
William C. Genne	Insurance Financial Examiner
Angela J. Graff	Insurance Financial Examiner
Frederick H. Thornton	Insurance Financial Examiner Advanced Exam Planning & Quality Control Specialist
Tim J. VandeHey	Insurance Financial Examiner Advanced Data Processing Audit Specialist
Elena V. Vetrina	Insurance Financial Examiner

Respectfully submitted,

John E. Litweiler
Examiner-in-Charge